# THE CONSTITUTION AND PUBLIC FRANCHISES

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NOTHING could make our paper constitutions and charters in America appear more futile—mere child's play—than to find in them sections or series of sections bravely prohibiting perpetual franchises and imposing whole pages of lucid restrictions upon franchise grants, when we know all the while that most of the actual franchises controlling the utilities in the commonwealth or the city for which the constitution or charter has been written have long since been bartered away in perpetuity and are in no respect subject to the restrictions imposed. So far as the framework of government is concerned, a new constitution or charter is effective in establishing the principles it declares. The old legislature, the old judiciary, the old counties, the old municipal departments, are superseded and displaced by the new, in so far as the constitution or charter calls for changes in the organization of government. But when we come to consider, not the forms of government, but its substantive acts, we find that a constitution drafted in 1915 is subordinate to a contract executed in 1914, or in 1814 for that matter. The result is that modern constitutions and charters, with their manifold and far-reaching provisions in regard to public utilities and public utility franchises, are often mere masks concealing rather than revealing the truth. In large measure they are theoretical and have no practical significance.

Where franchises are granted in perpetuity, a city does not have to be very old or very large before the power to control its public utilities through charter provisions or constitutional amendments applying only to the future is lost forever. Even in the case of street railways, where franchises are usually granted for specific streets rather than for all the streets within the limits of a given municipality, the early grants are almost uniformly on the down-town thoroughfares in the

strategic locations, with the result that they command the future development of transit facilities almost as much as if they covered all the streets of the municipality and were exclusive. Competition is a wholly inadequate remedy. Competition of street railways in the same streets, even though temporary, has long since been regarded as impracticable and intolerable except under extraordinary conditions. Competition in water supply and gas service, involving as it does the construction of duplicate systems of mains and the wanton tearing up of pavements and consequent interference with ordinary street traffic, is almost as unbearable as competition in street railways. In electric light and power and in telephone service, the disadvantages of competition from the standpoint of the street itself are serious, but not so forbidding under ordinary circumstances as in the case of the other utilities mentioned. From the standpoint of the public, however, competition in telephone service is theoretically intolerable, while in electric service it may have some immediate advantages.

Under the Dartmouth College decision, a private charter granted by a sovereign state becomes an inviolable contract, unless by specific reservation the grant is subject to amendment or repeal by the granting authority or its successors. In New York, where this reservation has been contained in the constitution for a great many years, the courts have distinguished between a corporation's charter and its special franchises, the latter being regarded in the nature of irrepealable grants of privileges, equivalent to the sale or gift of property, which, once made, is beyond recall by the city. This distribution, coupled with the ruling that a franchise or consent for the construction of public utility fixtures in the streets, unless specifically limited in the grant or in the laws under which the grant is made, is to be construed as being in perpetuity, has resulted in the intrenchment of public service corporations in the streets of New York so as to make their dislodgment extremely difficult.

The constitution makers have this practical situation to face. The principal streets, and in some cases all the streets, of the municipalities have been mortgaged in perpetuity to some or

all of the principal utilities, with the result that a prohibition of perpetual franchise grants written into the constitution in 1915 might remain there for a thousand years without having any direct effect upon the rights of the principal public service corporations operating in the cities now in existence, no matter how large those cities may become. Constitutions may come and constitutions may go, but Jake Sharp's Broadway franchise goes on forever, and the Eighth and Sixth Avenue purchase clauses have been abrogated for all time.

This situation is intolerable. To make a written constitution a lie is to make a mockery of our most fundamental political enactments. It not only violates the pride of self-respecting citizens of a free state, but it gives the state itself a false position in recorded history. But in addition to this sentimental and ethical reason, a constitutional provision that ignores the past and applies only to the future, that leaves the great body of public utilities unaffected and touches only the comparatively insignificant extensions and new experiments which need new franchises, creates a practical condition that defeats its own purpose. The streets of New York cannot remain permanently nine-tenths slave and one-tenth free. Short-term and indeterminate franchises do not mix with perpetual franchises. Restriction of future grants, while past grants remain unlimited, merely creates a deadlock in the development of the utilities and results in hardship to the public. It checks expansion by increasing the risk of new investments. It compels the slender outermost branches of the utility tree to carry heavier burdens than the strong trunk itself.

If perpetual franchises have proved to be contrary to public policy and a menace to the state, then the makers of the new constitution should not be satisfied to leave this menace as formidable and as threatening as ever, while at the same time depriving the people of the state of the slender advantages which may be claimed for the old system. Public utility corporations enjoying perpetual franchises will not accept partial re-locations advantageous both to the public and to themselves, if such re-locations involve the exchange of perpetual for limited rights. They will not permit the civic blacksmiths to

insert a twenty-five year link in a perpetual chain. They are very loth indeed to allow twenty-five year links to be welded onto the ends of their perpetual chain. As a result, a city, where the heart of its utility system has been constructed under perpetual franchises, finds that the enactment of stringent restrictions in regard to the grant of new franchises intensifies its distress. It is hard enough under any kind of a franchise to induce public utility corporations, operating for profit, to expand their lines as rapidly as the needs of the public demand. But when extensions and possible competing plants are made subject to stringent regulations not applying to the old lines having the cream of the business, then this reluctance is translated into violent and persistent refusal.

If restrictions are to be imposed upon future franchise grants, the only reasonable and safe policy for the state to adopt in its constitution is a policy looking toward the gradual extinguishment of all outstanding franchise rights and the substitution therefor of new grants under the restrictions considered proper for the future. Nothing is more absurd than the attempt to develop and operate a public utility under a multiplicity of conflicting franchises, and certainly the greatest absurdity of all is the attempt to leave undisturbed the perpetual franchises at the heart of the city and to develop the utility by piecing on short-term or indeterminate franchises at the extremities. It is equally futile to attempt to dislodge an intrenched utility by the doubtful expedient of private competition, when the competitor, in addition to the normal disadvantages he would have to meet in breaking into a new field and building a plant under more difficult conditions than his older rival originally had to meet, is put to the disadvantage of having a less favorable franchise and a shorter lease of life within which to recover his investment.

A constitution serves a double function. First, it organizes the government, adjusts conflicting political interests, and brings into action the constructive spirit of democracy. Second, it protects the future against exploitation by the present.

In the performance of the first of these functions, the constitution establishes the organs of state and local government,

differentiating so far as seems necessary their spheres of action, and confers upon them power to act on behalf of the organized public. So far as public franchises are concerned, the constitution must confer the franchise-granting power upon either state or local organs of government, and the right to own and operate public utilities will be similarly conferred unless it is expressly denied. If cities are to have any power in regard to franchises or public utilities except as it may be delegated to them by the legislature, such power must be conferred directly by the constitution. If the legislature is to be prevented from granting local franchises, then the constitution must make this restriction explicit. In the protection of the future from exploitation by the present, the constitution must impose limitations upon all contracts executed by any agent of the people, whether state or local. It certainly would be unintelligent to prohibit the legislature from granting perpetual franchises while permitting the municipality to grant them, or *vice versa*.

We may assume for the purposes of this discussion that the main outlines of the frame of government will remain the same under the new constitution as under the old. We shall doubtless continue to have a state legislature as well as cities, villages, counties and towns organized for local governmental and administrative purposes. The privilege of using public streets as rights of way for public utility fixtures will be obtained from the legislature, from some commission exercising delegated powers, or from the local authorities, or possibly from all of them.

Hitherto in New York the constitution has left to the state legislature the franchise-granting power and the power to acquire, own and operate public utilities, to be exercised or delegated as the legislature may see fit, subject to a very few limitations. Under section 18 of article III of the present constitution the legislature may not pass a private or local bill granting to any corporation, association or individual, the right to lay down railroad tracks or granting to any private corporation, association or individual any exclusive privilege, immunity or franchise. All such grants must be by general

law. But the legislature is further prohibited from authorizing the construction or operation of a street railroad except upon condition that the consent of the local authorities having control of the streets be obtained and also that the consent of the abutting property owners be secured, or, in case of their refusal, the consent of the appellate division of the supreme court, upon the recommendation of special commissioners appointed to inquire into the necessity of the construction of the railroad. There is nothing in the constitution limiting the duration of franchises, and nothing to prevent the legislature from granting franchises other than street railroad franchises by general law without the consent of either the local authorities or the abutting property owners. There is nothing in the constitution to prevent the legislature from passing laws to provide for the regulation, acquisition, construction or operation of public utilities, either by the state itself or by the municipalities; but the constitution does not itself give the cities the right either to regulate or to own and operate public utilities, or to grant franchises therefor. The requirement that the construction or operation of street railways may not be authorized without the consent of the local authorities is purely negative. It confers no actual franchise-granting power upon the cities, and no street railways could be built except under general state laws authorizing their construction.

As a matter of fact, many of the most important perpetual street railway franchises of New York city, and perhaps of other cities of the state, were originally granted in perpetuity by special acts of the legislature, prior to the time when the existing constitutional restrictions were adopted, and even since that time the legislature has granted perpetual gas franchises in New York city. But for many years it has been customary to require the consent of the local authorities for the construction in the public streets of most classes of utilities. It has always been doubtful, however, to what extent cities have the right to go, even in connection with the construction of street railways, in imposing terms and conditions in their franchise grants. This doubt has been so serious that the city of New York, under its special charter, re-

duces every franchise grant to the form of an elaborate contract to be executed by the grantee and protected by stringent and easily enforced penalties. Even with these precautions, there remains a doubt as to the validity of some of the conditions imposed.

One practical question to be determined by the constitutional convention is whether or not it will be advisable to confer larger constitutional guaranties upon cities with reference to the control of their streets and the regulation or ownership and operation of public utilities. This question is a part of the larger question of municipal home rule.

Many advocates of home rule lay stress upon the importance of giving cities the right to frame their own charters, including particularly the right to organize their local government. This right would permit them to choose the mayor-and-council plan, the commission plan, the city-manager plan, the federal plan, or any other plan of organization that seemed to the people of the city best suited to their local purposes and conditions. It might also secure to any city framing its own charter the right within certain limits to describe its own powers and functions. How far this latter right would be secured in this way would depend upon the particular wording of the home-rule charter provision as well as upon the interpretation of it by the courts, and probably would also depend upon the future action of the legislature by general laws. At best, the plan merely to grant cities the right to frame their own charters lays the principal emphasis on the form of local government and leaves the extent of the powers and functions of the cities uncertain and subject to future determination. This plan gives the husk but not the kernel of municipal home rule—the shadow but not the substance.

The fundamental trouble that has given rise to the municipal-home-rule movement in this country is well understood by students of municipal affairs. At the bottom of it is the old rule of American law that a municipality is a corporation having enumerated rather than general powers. Under this theory a city may not do anything except what it has been expressly authorized to do by legislative act. This means that

whenever a particular city wants to do anything, it has to inquire whether or not the right to do this thing has been conferred upon it, and if the right has not been conferred, then the thing cannot be done until the city's charter has been amended by vote of the legislature. Where special acts are prohibited, it is likely to be even more difficult to secure the new power desired than it is where special legislation is still in vogue.

The new theory of municipal government upon which the home-rule movement is founded is that a city should be a corporation of general powers, having the right to do anything it sees fit to do for the protection, welfare and government of its inhabitants, unless there is some specific provision of the constitution or the statutes prohibiting it from taking such action. At the bottom of the home-rule movement is this desire to reverse the rule of law with reference to the powers of municipalities in this country. It appears that this rule cannot be effectively reversed except by constitutional guaranties. Therefore, an essential part of the home-rule program, so far as the constitution is concerned, is the grant to all cities of broad powers of local self-government and self-help. But the courts are so jealous to protect the sovereign powers of the state government, and the relations between state and municipal functions are so intricate and confused, that a home-rule constitutional provision, in order certainly to be effective, must be comprehensive and specific, so far as the most important municipal functions are concerned. This is especially true with reference to public utilities, where enormous vested private interests are involved.

The importance of making this grant specific has been recognized in recent years by such great commonwealths as Michigan, California and Ohio.

The new constitution of Michigan, adopted in 1908, contains the following provision (art. 8 sec. 23):

> Subject to the provisions of this constitution, any city or village may acquire, own and operate, either within or without its corporate limits, public utilities for supplying water, light, heat, power and

transportation to the municipality and the inhabitants thereof; and may also sell and deliver water, heat, power and light without its corporate limits to an amount not to exceed twenty-five per cent of that furnished by it within the corporate limits; and may operate transportation lines without the municipality within such limits as may be prescribed by law: Provided, That the right to own or operate transportation facilities shall not extend to any city or village of less than twenty-five thousand inhabitants.

In 1911, California adopted a series of important amendments to its constitution. One of these conferred the right to own and operate public utilities upon all the municipal corporations of the state. This provision, as amended in 1914, is as follows (art. 11 sec. 19):

Any municipal corporation shall have power to acquire by purchase, lease, condemnation or otherwise, in whole or in part, or to construct, and to own, maintain, equip and operate public utilities; and to grant franchises to persons, firms or private corporations to establish, equip, maintain and operate public utilities, upon such conditions and under such regulations as may be prescribed under the organic law of such municipality or otherwise by law. Any municipal corporation may furnish the product or service of any public utility conducted or operated by it to other municipal corporations and the inhabitants thereof, and to consumers and users outside of its limits.

The Ohio constitutional convention of 1912 submitted a long series of amendments. One of those related to "Municipal Corporations." The following sections were adopted as a part of this amendment (art. 18 sections 4 and 6):

Sec. 4. Any municipality may acquire, construct, own, lease and operate within or without its corporate limits, any public utility the product or service of which is or is to be supplied to the municipality or its inhabitants, and may contract with others for any such product or service. The acquisition of any such public utility may be by condemnation or otherwise, and a municipality may acquire thereby the use of, or full title to, the property and franchise of any company or person supplying to the municipality or its inhabitants the service or product of any such utility.

Sec. 6. Any municipality, owning or operating a public utility for the purpose of supplying the service or product thereof to the municipality or its inhabitants, may also sell and deliver to others any transportation service of such utility and the surplus product of any other utility in an amount not exceeding in either case fifty per centum of the total service or product supplied by such utility within the municipality.

The demands of the municipal-home-rule program will not be satisfied if the cities of this state are merely given the nominal or formal right of municipal ownership. In order to be effective as an element of real local self-government, the right must be explicit and practically available for use. One of the greatest difficulties in the way of the practical use of the right of municipal ownership is the financial one. Most cities are heavily indebted, and no one proposes to do away entirely with the constitutional limitation upon municipal debt. It is clear, however, that the right to own and operate public utilities is not worth the paper it is written on unless a city has within its grasp some means of paying for them, whether they are acquired from an existing company or constructed new.

The new Michigan constitution provides that the legislature shall enact general laws limiting the rate of taxation for municipal purposes and restricting the powers of cities in borrowing money and contracting debts. It further provides that whenever a city is authorized to acquire or operate a public utility, it may issue mortgage bonds for the purpose beyond the general limit of bonded indebtedness prescribed by law. Such bonds, however, are not to impose any liability upon the city, but are to be secured only upon the property and revenues of the utility, including a franchise for not more than twenty years to be available for use in case of foreclosure by the bondholders. Under this provision, the legislature has granted a two per cent margin of indebtedness to be incurred against the general credit of the city for public utility uses, thus reducing far below the cost of construction or acquisition the amount of bonds necessarily issued against the utility property itself. Under this provision, the city of Detroit is now

proceeding to acquire the local street railway system. The same provision with regard to the issuance of bonds in excess of the general debt limit was included in the new constitution of Ohio.

These provisions are much more favorable to municipal home rule than the existing provisions contained in section 10 of article 8 of the constitution of New York relating to the debt limit. Under the New York plan, water bonds, issued after certain specified dates, are not to be included in the debt limit, and so far as the city of New York is concerned, debts incurred for the construction of other public utilities, although they must come within the debt limit in the first instance, subsequently may be excluded therefrom for such period of time as the utilities shall be self-sustaining, provision for the amortization of the bonds by the time they fall due included. Under this provision as it relates to the city of New York it would be absolutely impossible to acquire any one of the principal utilities, unless such a utility could be acquired piecemeal. Even then, this would hardly be possible unless the gap between the city's debt and the constitutional debt limit were considerably greater than it shows any indication of being. It is apparent, therefore, that if this central provision of the municipal-home-rule program is to be anything more than a false promise, it must be buttressed by a practical release of municipal credit for public utility purposes going far beyond the provisions of the present constitution of this state.

When we consider the enormous capital invested in privately owned public utilities and the huge addition to municipal debts that would result from the outright purchase of these utilities by the cities, it becomes apparent that something more than the mere right to purchase and even something more than the release of the cities' credit for the purpose of purchase may be required.

The city of New York now imposes heavy special taxes upon public service corporations. This has been done partly because these corporations, operating for the most part under perpetual franchises, were believed to be making excessive profits for their private owners, although their franchises had

in most cases been given to them free. The proceeds of these taxes, and of other special taxes which may be levied upon public utilities in the future, might well be put aside into a fund for the extinguishment of such outstanding franchise rights as cannot be brought under control in any other way.

In so far as new franchises are important, it is clear that the interests of the cities cannot be properly protected unless the franchise-granting power is guaranteed to them. It is coming to be recognized more and more that the most practical method by which most cities may acquire public utilities is by means of franchise or rate contracts under which the companies will be authorized and required gradually to withdraw their capital out of earnings and thus gradually reduce the price at which the city may purchase their property. It is essential to municipal home rule that the cities should have the power to enter into such contracts.

Perhaps it is necessary in this discussion to present the reasons why the right to own and operate public utilities and to control franchises granted therefor should be granted to the cities. Public utilities, in the narrow sense, are primarily services essential to urban life and economically available only under urban conditions. It is true that in recent years many of the utilities have been branching out, extending into the suburbs, running from town to town, and in some cases spreading into rural regions; but almost without exception these utilities depend for their success upon the use of city streets and the service of congested districts. So far as they go to the country, they are merely carrying to it some of the benefits of urban life. Essentially a public utility is an urban institution. It, more than any other form of urban activity, embodies the principle of coöperation both in demand and in supply that makes modern urban life on a large scale possible. Public utilities are in their essential features, therefore, still local. It is the city that is primarily interested in the structure, rates, service and extension of the street railway, gas, water or electric plant or the telephone system that serves it. Home rule would certainly be an empty name if the cities were stripped of all power to control the development of public utilities.

This brings us to a consideration of the interests of the state in the control and development of public utilities and of the relations of cities to each other and their suburbs in connection with such control and development. While utilities are primarily local, it cannot be denied that there is a wide field for uniform state control of public service corporations. It is also clear that under modern conditions, where many utilities operate in more than one community, some adjustment of the control exercised by different local authorities must be made. It is doubtful whether the time is ripe for the inclusion in the constitution itself of an elaborate analysis of these problems. This seems to be the province of statutory rather than constitutional law. If we are to reserve to the cities the right to acquire, own and operate public utilities, made practical by the release of municipal credit, and the right to prescribe the terms and conditions upon which franchises for the use of city streets shall be granted, subject possibly to a review by a state commission or court where the interests of other municipalities appear to be involved, the essential features of the home-rule program with reference to franchises and public utilities will be realized.

It goes almost without saying that the granting of perpetual franchises to private parties for the use of the public streets should be prohibited, but this prohibition will be futile in the extreme unless it is supplemented by additional restrictions upon the duration and character of franchise grants. A constitutional provision under which Buffalo's 999-year franchises could be granted while the perpetual franchises of New York city could not be, would establish a distinction without a difference. Not only should the granting of new perpetual franchises be prohibited, but the perpetual franchises already outstanding should be declared inimical to public welfare and contrary to awakened public conscience and the permanent public policy of the state. Penalties should be established and rewards offered calculated to recover for the state and its cities the control of outstanding franchises.

In the first place, the constitution should give backbone to the rule, better known in New York judicial proceedings by its

violation than by its enforcement, that all grants of special privileges in the public streets are to be construed strictly in favor of the public. The constitution should also provide that no further grant of powers or privileges shall be made to any public-service corporation except upon the surrender of its present claims to perpetual or practically perpetual franchises. It should provide that no new franchise shall be granted and no readjustment of existing franchises made without a reservation to the city or the state of the right to acquire the property of the utility at the expiration of a fixed period not to exceed 20 or 25 years at the most, or at any time thereafter, without paying for the surrender of the franchise itself. Where the franchise is for the passage of a railroad or other utility rendering through service only, the option to purchase should be reserved to the state. The limitation upon franchise grants should apply to trunk-line railroads, power transmission lines, gas and oil supply conduits and long-distance telephone lines as well as to the more strictly local utility structures, but the state should be substituted for the city as the beneficiary of such restrictions in the case of through-service utilities.

Eternal vigilance is the price of liberty—after we get it. But to get it we have to pay something more. Even after perpetual franchises have been outlawed, the *posse comitatus* will have quite a job catching them. The thing of real importance is not the mere form and duration of franchise grants. These are the husks. The real thing is the investment in public utilities. The price we shall have to pay for getting our liberty, which, when we get it, even a paper constitution will help us keep, is the definite recognition that public utilities are public servants and that money invested in them is not a permanent private investment but a temporary investment in aid of public credit. This means that the state's and the city's protection should be extended to legitimate public utility investments. Such protection is the logical result of the public-agency theory of public utility operations. Both the protection and the theory are incompatible with the existence of perpetual franchises vested in private corporations.

Michigan, in its new constitution, limits term franchise grants to thirty years. Limitations of the same general nature are contained in the statutes of many states. But none of the states as yet provides an entirely satisfactory substitute for the perpetual franchise. The theory of the perpetual franchise is that the investment in public utilities is a permanent one, which need not be diminished or retired, and that the ownership and operation of public utilities as private property is the permanent policy of the state. This theory has the advantage of being thoroughly logical and consistent. The theory of franchises whose duration is limited to a specified period of time, without any guaranty as to the future of the property invested under their protection, is dubious and inconsistent with the established nature of public utilities. Certainly, the needs of the people require that public utilities shall continue to operate and to expand with the increase of urban population, without reference to the dates for the expiration of franchises. Public utilities must be provided and developed for continuous service. A term franchise that gives the corporation no guaranty of its investment after the expiration of the grant operates directly counter to the public interest. The owner of the franchise, if a conservative financial policy is to be followed, will see to it that the consumers not only pay operating expenses and interest on investment, but also repay the investment itself within the period of the grant. The owner then is in the happy position where he cannot lose, and stands to gain the entire value of the property in case the city concludes either to purchase the property or to renew the franchise, as it is morally certain to do. The indeterminate franchise, as established in the laws of Wisconsin and Indiana, grants rights in perpetuity, subject only to the power of the municipality in its discretion to terminate the grant at any time upon taking over the property of the utility at a price to be fixed by the state commission. The theory of the indeterminate franchise of the Wisconsin type is that the investment in public utilities is a permanent one and does not need to be retired out of earnings, but that the question of private or public ownership is one to be kept open for future determination by the city. This

type of franchise, from the public standpoint, is much superior to the perpetual franchise, and from the investor's standpoint it is much superior to the limited-term franchise. Its great drawback is that it settles the franchise problem once for all until such time as the city is prepared to take over the property of the utility and pay for it a sum to be determined by the state commission. Technically, the Wisconsin plan abolishes perpetual franchises, but does not take any definite steps toward the municipalization of public utilities. It provides no means by which the financial difficulty of paying for utilities and retiring the private investment therein may be lessened. The indeterminate franchise tends to quiet the relations between the people and the utility. There is no regularly recurring period when the obligations of the utility to the city are subjected to a new scrutiny.

Summarizing this discussion, I maintain that the new constitution of the state of New York should contain the following provisions:

1. A provision specifically conferring upon all cities the right to acquire, own and operate public utilities within or without their corporate limits, the exercise of such right outside of the corporate limits being subject to supervision by a state commission.

2. A provision authorizing cities to issue bonds outside the general debt limit upon the security of the property and revenues of utilities owned by the city.

3. A provision conferring upon cities the franchise-granting power and making the action of the cities final except as to franchises to be used merely for through service. In the case of the latter, the refusal of the municipality to grant the franchise, or the conditions upon which the franchise is granted, should be subject to review by a state board.

4. A provision prohibiting the grant of perpetual franchises, and requiring that all franchises be granted subject to the right of the city or of the state to take over the physical property of the utility upon making proper compensation for such property.

5. A provision forbidding the grant of additional franchises, powers or privileges to corporations or individuals claiming perpetual or very long-term franchises, except on condition that such claims be surrendered and that new franchises, in accordance with the spirit and the letter of the new constitution, be accepted in their place.

6. A provision prohibiting the opening or acceptance of a public street subject to public utility easements previously granted by the owners of the land.

7. A provision prohibiting the recognition of perpetual franchise rights except on clear proof that such rights were granted by a formal recorded act of the proper authorities and in strict compliance with the law, and that such rights have not been forfeited by non-user, misuse or failure to comply with the terms and conditions of the grant.